

Local trusts versus offshore trusts

This table summarises the most pertinent practical similarities or differences between a locally-registered inter vivos trust and one registered in one of the many tax-friendly foreign jurisdictions.

	South African trust	Offshore trust
Why set up a trust?	The accumulation of wealth in trust provides for continuity, the protection of assets and the smooth transition of assets from one generation to the next. It may also lead to significant savings in estate duty and related administration costs on death when used timeously and effectively.	
Formation	<p>The founder/donor enters into an agreement with the trustees (referred to as the trust deed), whereby the trustees undertake to administer the trust assets for the benefit of the beneficiaries.</p> <p>The trustees will accept their appointment and the trust will then be lodged with the Master of the High Court.</p> <p>The Master will issue a Letter of Authority to confirm who the trustees are and they will subsequently be authorised to act on its behalf.</p> <p>Local trusts established in terms of South African law fall under the law of contract and are a contract for the benefit of a third party (stipulatio alteri).</p> <p>In the context of an inter vivos discretionary trust, the trustees are the legal owners of the trust property, which they own for the benefit of the beneficiaries of the trust.</p>	<p>The person establishing the trust is referred to as the settlor (rather than the founder/donor as is the case with local trusts).</p> <p>The settlor will instruct the formation of the trust to the trust company.</p> <p>A settlement deed/declaration of a trust will be drafted outlining the terms and conditions of the trust, which most often only the trustee signs.</p> <p>Offshore trusts established in terms of the Common Law recognise a concept of dual ownership whereby the trustee is the legal owner of the trust property while the beneficiaries are the beneficial owners thereof.</p>
Parties to the trust	<p>Founder/donor</p> <p>Trustees</p> <p>Beneficiaries</p>	<p>Settlor</p> <p>Trustee</p> <p>Beneficiaries</p> <p>Protector</p>
Founder/Settlor	<p>In general, the founder plays a relatively small role in the trust.</p> <p>The trust deed can provide for certain powers.</p> <p>In many instances, the founder is also one of the trustees.</p>	<p>The settlor plays no role in the trust, other than initiating the creation thereof.</p> <p>The settlor is responsible to appoint the protector.</p>

South African trust**Offshore trust**

	South African trust	Offshore trust
Trustees	Both trusts require a trustee(s) to administer and manage the trust assets for the benefit of the beneficiaries. The trustees have a fiduciary duty towards the beneficiaries of the trust.	
Trustees	<p>The trust deed will determine the minimum number of trustees.</p> <p>One of the important differentiators between local and offshore trusts is that the founder/donor often appoints him- or herself as a trustee together with a spouse and other persons known to the founder.</p> <p>To ensure total divestment of trust assets from the estate of the founder/ estate planner and good governance, it is a requirement supported by case law that one of the trustees is an independent trustee who does not benefit from the trust in any way.</p> <p>In most instances, the independent trustee is a professional trustee who undertakes the day-to-day administration of the trust.</p>	<p>The settlor cannot be a trustee. The tax residency of the settlor will influence the tax liability of the trust and therefore the trustee is limited to a trust company in that foreign jurisdiction.</p> <p>That trustee controls the trust assets and makes all the decisions regarding the trust assets.</p> <p>The settlor can write a Letter of Wishes that informs the trustees of their wishes insofar the management and distribution of trust assets.</p> <p>Even though the Letter of Wishes is not legally binding on the trustee(s), in practice trustees will follow its direction unless there are valid reasons not to.</p>
Beneficiaries	<p>The trust deed will define who the beneficiaries are.</p> <p>It is necessary that the beneficiaries can be determined with certainty.</p>	<p>The trust deed generally provides the trustee with the power of appointment whereby they can add or remove beneficiaries and declare a beneficiary to be an Excluded Person.</p> <p>They will, however, follow the direction of the settlor and the direction in the Letter of Wishes.</p>
Protector	Not applicable to South African trusts.	<p>The settlor can appoint the protector to oversee the administration and the actions of the trustees.</p> <p>It is generally someone that the settlor trusts.</p> <p>The protector can also have veto rights to overrule some decisions of the trustee and can even have the right to remove the trustee.</p> <p>The protector cannot be a beneficiary of the trust.</p>
Funding the trust	Most trusts are funded by way of a donation or an interest-free loan that the donor made to the trust.	

South African trust

Offshore trust

Tax: Funding

Where a donation is made, donations tax will be payable at 20% (or 25% for donations made above R30 million) on the amount exceeding R100 000 per year where the donor is a natural person.

Where an interest-free or low-interest loan is made to the trust, Section 7C of the Income Tax Act will apply.

Insofar as the interest rate charged on the loan is less than the official interest rate (repo rate plus 1%), it will be treated as a deemed donation that the lender made to the trust and therefore subject to donations tax.

The tax implications will be similar to that of the local trust. However, SARS can view the funding transaction as an affected transaction as defined in Section 31 of the Income Tax Act, in which case transfer pricing adjustments can be made. If this is the case, Section 7C will not apply to that loan.

Tax: Income or capital gains earned

If the income is taxable in the trust, it will be subject to a fixed rate of 45%. However, if the trust was funded by way of a low- or no-interest loan, the provisions of Section 7(5) will deem the income earned by the trust to be that of the donor and it will be included in the gross income of the donor. Similar attribution rules apply if capital gains are realised in the trust.

Where the trustees decide to vest the income or capital gains in a resident beneficiary, Section 25B will apply resulting in the income/gain retaining its nature in the hands of the beneficiary and then being taxable in the hands of the beneficiary.

The tax consequences to the settlor will be similar to that of the South African trust if the trust is funded by a low- or no-interest loan, even though the income/capital gains are earned/realised in the offshore trust.

If, however, the income/gain vests in the trust, there is generally no tax payable in the jurisdictions used by most South African clients.

The views and/or opinions expressed in this article have been prepared as a primary source of information and are not a recommendation for the conclusion of a transaction. This article has been prepared for general information and not having regard to any particular person's financial planning, tax planning, investment needs and objectives. The information used to prepare this document includes information from third-party sources and is for information purposes only. Although reasonable steps have been taken to ensure the validity and accuracy of the information contained herein, Momentum Metropolitan Life Limited does not guarantee the accuracy, content, completeness, legality or reliability of the information contained herein and no warranties and/or representations of any kind, expressed or implied, are given to the nature, standard, accuracy or otherwise of the information provided. Neither Momentum Metropolitan Life Limited, its affiliates, directors, officers, employees, representatives or agents (the Momentum Parties) have any liability to any persons or entities receiving the information made available herein for any claim, damages, loss or expense, including, without limitation, any direct, indirect, special, incidental, punitive or consequential cost, loss or damages, whether in contract or in delict, arising out of or in connection with information made available herein and you agree to indemnify the Momentum Parties accordingly.

Any unauthorised copying or reprinting or publishing in any other publications, webpages or emails is strictly prohibited. Should you wish to use this article for any such purpose, please email sharon.hamman@momentum.co.za to obtain permission.

Momentum Investments is part of Momentum Metropolitan Life Limited, an authorised financial services (FSP6406) and registered credit (NCRCP173) provider